

COMPETITION IN ILLINOIS RETAIL ELECTRIC MARKETS IN 2003

ILLINOIS COMMERCE COMMISSION

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Executive Summary

Sec. 16-120(b) of the Public Utilities Act (“Act”) directs the Illinois Commerce Commission (“Commission”) to submit an annual report to the Joint Committee on Legislative Support Services of the General Assembly and the Governor that provides information concerning the development of competitive electricity markets in Illinois. This is the fourth report the Commission has submitted to the General Assembly pursuant to this section of the Act.¹ The Sec. 16-120(b) reports will continue to the end of the “mandatory transition period” in 2006.

Sec. 16-120(b) requires the Commission to furnish certain statistical information concerning power and energy sales by electric utilities and also by Alternative Retail Electric Suppliers (“ARES”) to customers eligible to select new electric suppliers. The Commission may also provide any other information the Commission believes is relevant in assessing the development of Illinois electric markets.

Retail Market Activities

The retail electric market opened in October 1999 to approximately one-third of all non-residential customers, comprising a total of about 64,000 customers. On January 1, 2001, all non-residential customers of the investor-owned utilities became eligible to choose alternative suppliers. The number of eligible non-residential customers is now about 500,000. An additional 4,440,000 residential customers became eligible for customer choice in May 2002.

Supply Options Available to Electric Customers

Customers have several supply options available to them from both the incumbent utilities and alternative suppliers. Customers may purchase bundled power and energy offered by the incumbent utilities at rates regulated by the Commission. These rates are frozen until 2007. Customers may also choose to purchase power and energy on an “unbundled” basis by switching the generation portion of their electric service to an ARES or from any electric utility serving outside its traditional service area. (Collectively, the ARES and electric utilities serving outside their service areas are called “Retail Electric Suppliers” or “RESs.”) Additionally, the two utilities (Commonwealth Edison and Illinois Power) that charge transition charges to customers who receive delivery services also offer an unbundled, market-based generation option called the “Power Purchase Option” (“PPO”). Unbundled power and energy, whether purchased from an ARES or from an electric utility under the PPO is delivered to customers under delivery services tariffs at rates regulated by the Commission.

¹ Previous reports submitted to the General Assembly pursuant to Sec. 16-120 of the Act can be viewed at <http://www.icc.state.il.us/ec/electricity.aspx>. These reports include the triennial reports filed pursuant to Sec. 16-120(a).

Approximately 19,600 non-residential customers were taking delivery services customers at the end of 2003. About 17,400 ComEd customers, or about 5.4% of ComEd's non-residential customers, had selected delivery services. About two-thirds of ComEd's delivery services customers are taking service from a Retail Electric Supplier ("RES"), while the remaining one-third is taking PPO service from ComEd.

Approximately 1,100 customers are taking delivery services in the Illinois Power service area. The vast majority of these customers are receiving PPO service from Illinois Power. About 500 AmerenCIPS customers have switched to delivery services. Each of the customers is purchasing electricity from RESs, since AmerenCIPS suspended its collection of transition charges in 2003 and thus does not currently offer PPO service. A small number of customers were taking service from Retail Electric Suppliers in the service areas of AmerenCILCO and AmerenUE at the end of 2003. No customers in other service areas are taking delivery services.

Retail Electric Supplier Activities

Eleven RESs sold power and energy to retail customers in 2003, one fewer than in 2002. One RES was certified in 2003, and one RES requested decertification from the Commission. RESs made sales in 2003 of about 20.6 million megawatt-hours ("mWh"). This total represents about 16.4% of sales to all retail customers.

As in prior years, RESs concentrated their marketing efforts in the ComEd area. Additionally, AmerenCIPS' suspension of transition charge collection has begun to attract new marketers to its service territory. However, there was no indication by the end of 2003 that RESs were actively marketing in any of the State's smallest service areas or were interested in marketing to residential customers.

Power Purchase Option Sales

In 2003, over 28% of the unbundled power and energy sales were PPO sales, a large drop from last year's 40% figure. The PPO is especially popular in the Illinois Power service area, where 97% of delivery services customers with a demand under one megawatt ("MW") was taking service under the PPO. The Commission has noted in prior reports that reliance on the PPO may be cause for concern for the long-term development of the market.

Peak Demand and Sales

The sum of the non-coincident peak demands of the nine investor-owned utilities totaled 29,946 megawatts. This total, which includes both unbundled and bundled customer demand, represents an increase in non-coincident peak demand of approximately 1.0% compared to 2003. Non-coincident peak demand grew at an annual growth rate of about 1.6% between 1991-2003, an increase of about 427 megawatts per year.

Wholesale Market Activities

Since the State's largest utilities have transferred or sold their generating facilities, the power and energy needed to serve their retail customers must be purchased from merchant generators in the wholesale market. Currently, these utilities have wholesale power contracts in place with the companies that now own the generating facilities, but the contracts will expire by January 1, 2007, when the retail rate freeze period terminates.

The Commission is concerned that the wholesale market will not be sufficiently competitive by 2007 to ensure that the power that utilities procure on behalf of their bundled customers will be reasonably priced. Moreover, the ultimate success of electric restructuring depends to a great extent on the competitiveness of the wholesale market. The Commission's evaluation of the wholesale market is described in the Commission's most recent Sec. 16-120(a) report.

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I. Introduction

Sec. 16-120(b) of the Public Utilities Act requires the Illinois Commerce Commission to submit an annual report to the Joint Committee on Legislative Support Services of the General Assembly and the Governor describing the development of electric competition in Illinois. Sec. 16-120(b) requires the Commission to furnish certain statistical information related to sales by electric utilities, both inside and outside their service territories, as well as sales by Alternative Retail Electric Suppliers ("ARES"). The statutorily required information is supplemented with other statistical information to illuminate the extent of competition in Illinois retail electric markets.

An examination of the switching statistics provided in the report shows indications of retail electric market growth in the service territories of the three largest utilities in the state. In the Commonwealth Edison ("ComEd") service territory, a relatively large number of customers have switched from ComEd's bundled service to delivery services, continuing a growth pattern that began as soon as the market opened to electric customers in October 1999. By the end of 2003, about 17,400 ComEd commercial and industrial customers had switched either to alternative supplier or to the Power Purchase Option ("PPO"), a market-based service that is available only to the customers of the utilities that assess transition charges. ComEd's introduction of a multi-year transition charge plan in 2003 encouraged larger customers to switch away from PPO service to RES supply.

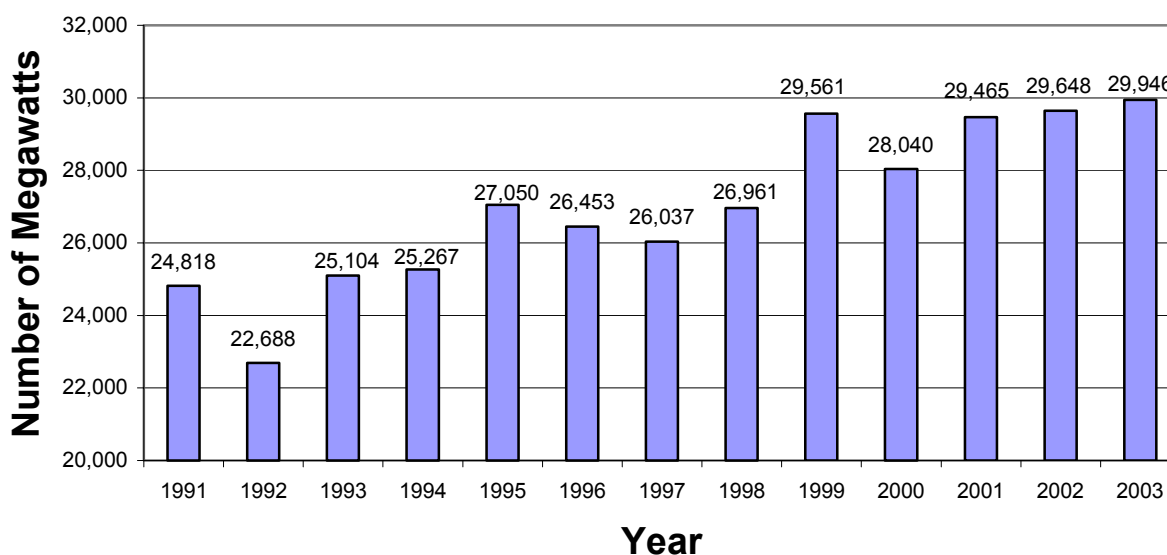
Several hundred customers have switched to delivery services in the service territories of AmerenCIPS and Illinois Power. Prospects for increased customer switching activity in the AmerenCIPS service territory looks particularly favorable, as AmerenCIPS suspended its collection of transition charges for at least two years. However, switching has been virtually non-existent in the service territories of the State's smaller utilities. After more than four years of customer choice, there are few signs that customers in those service areas will have supply options other than the bundled service offerings provided by utilities.

II. Peak Demand and Sales by Electric Utilities and ARES

A. Peak Demand Statistics

Sec. 16-120(b) directs the Commission to present information concerning peak demand in the service territories of the investor-owned utilities. Figure 1 shows the level of non-coincident peak demand between 1991 and 2003. Non-coincident peak demand in Illinois has grown at an annual rate of about 1.6% since 1991, an increase of about 427 MW annually.

Figure 1: Illinois Investor-Owned Electric Utility Non-Coincident Peak Demand, 1991-2003 (Megawatts)



B. Electric Sales By Electric Utilities and ARES

Sec. 16-120(b)(2) requires the Commission to collect data concerning the following:

The total annual kilowatt-hours delivered and sold to retail customers in the State of Illinois by each electric utility within its service territory, each electric utility outside its service territory, and alternative retail electric suppliers in the preceding calendar year.

Sec. 16-120(b)(3) requires the Commission to express the information collected in response to Sec. 16-120(b)(2) in percentage terms. Together, these two subsections provide an indication of the marketing success alternative suppliers have achieved since the retail market opened in October 1999.

The Commission gathered information from the utilities and ARES concerning their electricity sales to retail customers during 2003. This information is summarized in Table 1. Total sales by electric utilities include the following: (a) bundled electricity sales; (b) "Contract Sales," which include sales under Sec. 16-106 and Sec. 16-116 of the Act, sales under "special rate contracts" that were entered into prior to the December 1997 enactment of the 1997 restructuring law, sales to delivery services customers under the incumbent utilities' delivery services tariffs and sales under "Interim Supply Service";² (c) PPO sales, including both "unassigned" and "assigned" sales; and (d) sales by electric utilities outside their service territories. The sales by ARES are electric sales to delivery services customers under the incumbent utilities' delivery services tariffs. The sales by electric utilities plus sales by ARES equal "deliveries."

Table 1 shows that by the end of 2003 the RESs (ARES and utilities serving outside their services areas) were serving a significant fraction of retail customers. Sales to all retail customers, including delivery services customers, totaled approximately 126.0 million mWh during 2003. The ARES' shares of these sales were about 14.6 million mWh, or 11.6% of all sales. Sales by utilities operating outside their service territories (AmerenCILCO, Illinois Power and MidAmerican) were approximately 6.0 million mWh, or 4.8% of all sales. Thus, sales by RESs equaled about 16.4% of all retail sales. This percentage represents about a 32% increase from 2002, when RESs obtained sales of about 12.4% of all retail sales. Part of the reason for the increase appears to be that RESs gained sales to customers that were formerly taking PPO service from AmerenCIPS and ComEd. An additional reason is that former special contracts customers switched to RES service as their contracts terminated. Overall, sales to retail customers decreased about 1.0% from 2002.

Table 1: Sales by Electric Utilities and ARES During 2003

<i>Sellers</i>	<i>Electric Utilities</i>				<i>ARES</i>
<i>Sales Category</i>	<i>Bundled</i>	<i>Contract</i>	<i>PPO</i>	<i>Outside Territory</i>	<i>Retail</i>
<i>Amount of Sales (Million mWh)</i>	87.2 ³	5.4	12.7	6.0	14.6

² Interim Supply Service is a tariffed short-term service available to delivery services customers who have no source of electric supply.

³Due to the small amount of switching in the AmerenCILCO service territory, RES sales are included in the Bundled Service category. Please see Docket No. 03-0712.

<i>Sellers</i>	<i>Electric Utilities</i>				<i>ARES</i>
<i>Sales Category</i>	<i>Bundled</i>	<i>Contract</i>	<i>PPO</i>	<i>Outside Territory</i>	<i>Retail</i>
<i>Percent of All Sales</i>	69.2	4.3	10.1	4.8	11.6

III. Retail Activity in 2003

In this section the Commission examines various indicators of the development of the Illinois retail electric market. Customer switching statistics are presented below in Tables 3-6 for the State's six largest utilities. Customer selection of the Power Purchase Option is discussed in Section III.B. Supplier activity is discussed in Section III.C.

A. Delivery Services Growth

Customer switching rates, as measured by customer movement from bundled service to delivery services, continue to be high in the ComEd region relative to other service territories. As shown in Table 3, a large percentage of customers and a significant amount of customer load have switched from bundled service to delivery services. At the end of 2003, about 17,400 ComEd customers were either taking service from a Retail Electric Supplier or service from ComEd under the PPO.⁴ The 17,400 customers represent about 46% of ComEd's total commercial and industrial load (see Table 3).

Customer switching activity is growing more slowly in the AmerenCIPS and Illinois Power service territories, the only other areas in which customers have switched to delivery services in non-negligible numbers. About 500 customers have switched to delivery services in the AmerenCIPS service territory, about a third less than in 2002. Each of these customers is taking service from a RES, as AmerenCIPS was permitted to suspend its offering of PPO service after the Commission approved AmerenCIPS' request to suspend its collection of transition charges for at least two years.

In the Illinois Power service territory, about 1,100 customers have switched to delivery services. Only 35 of Illinois Power's delivery services customers were being served by RESs. However, these customers comprise about 31% of Illinois Power's total usage.

⁴ These totals exclude the 48 Governmental customers and 2,150 "Other" customers that switched to delivery services.

Table 2: Number of Delivery Services Customers in 2003

<i>Utility/Demand Level</i>	Number of Customers Eligible for Delivery Services		Number of Customers Switched to Delivery Services		Percentage of Customers Switched to Delivery Services (%) ⁵	
	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>
AmerenCILCO	23,240	89	0	-	0	-
AmerenCIPS	47,921	152	469	43	0.0	0.0
AmerenUE	7,525	37	2	0	1.0	0.0
ComEd	321,341	1,394	16,422	996	5.1	71.4
Illinois Power	66,259	215	1,032	77	1.6	35.8
MidAmerican	1,298	16	0	0	0.0	0.0
Total	467,584	1,903	17,926	1,116	3.8	58.6

Table 3: Amount of Usage Switched to Delivery Services in 2003

<i>Utility/Demand Level</i>	Amount of Usage Eligible for Delivery Services (Thousand mWh)		Amount of Usage Switched to Delivery Services (Thousand mWh)		Percentage of Usage Switched to Delivery Services (%) ⁶	
	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>
AmerenCILCO	1,495	1,852	0	-	0	-
AmerenCIPS	2,574	3,125	174	1612	6.8	51.6
AmerenUE	663	1,855	2	7	0.3	0.4
ComEd⁷	28,515	26,328	10,248	15,217	35.9	57.8
Illinois Power	4,691	8,079	736	4,843	15.7	59.9
MidAmerican	485	371	0	0	0.0	0.0
Total	38,423	41,610	11,160	21,678	30.2	54.5

B. Power Purchase Option

Tables 4 and 5 show that about 30% of ComEd's delivery services customers have switched to the PPO. The percentage of customers taking PPO service in the ComEd area dropped from about 40% in 2002 after ComEd introduced a tariff allowing larger customers to lock-in a multi-year transition charge. This tariff had the effect of encouraging customers to forgo their reliance on the PPO and instead sign multi-year contracts with suppliers.

⁵Percentages do not include AmerenCILCO data.

⁶Percentages do not include AmerenCILCO data.

⁷ Usage totals exclude the 3,668 Million kWh consumed by Governmental and Other customers.

AmerenCIPS suspended its transition charge tariff in 2003, which enabled it to drop its offering of PPO service. In 2002, about 554 customers were taking the PPO. Some of these customers switched to Retail Electric Suppliers and others returned to AmerenCIPS' bundled service after the PPO no longer was available. In the Illinois Power service area, PPO service is by far the most popular delivery service. Almost 99% of Illinois Power delivery services customers under one MW were taking PPO service at the end of 2003 and about 80% of IP's larger-use delivery services customers have switched to the PPO.

The Commission has noted in previous Sec. 16-120 reports that the popularity of PPO service can be viewed as an unfavorable sign of the prospects for the long-term development of a competitive retail market. From one viewpoint, the existence of the PPO allows customers to receive a rate discount even when no suppliers are serving the market. The PPO also allows suppliers to gain a market foothold and establish customer relationships because suppliers can essentially resell the utility's PPO to customers, either as a "billing agent" or through the "PPO Assignment" provisions of Section 16-110 of the Act. On the other hand, suppliers and customers can rely on PPO service only until the end of 2006.⁸ It is also evident that the PPO could vanish as a customer supply option prior to 2006 if a utility forgoes the collection of transition charges, as AmerenCIPS did in 2003. Once the PPO ceases to be a service offering, the customers who have found the PPO a convenient way to receive a rate discount without having to take a step into the market may well discover that they have to return to the higher-priced bundled service, unless they are fortunate enough to find a RES who is willing and able to offer a competitive price. Moreover, there is no guarantee that traditional bundled service will always be available to customers, as provisions in the Act permit utilities to petition the Commission to declare power and energy competitive, which could result in utilities dropping bundled service for some customers.⁹

Table 4: Selection of Power Purchase Option During 2003

	Number of Customers Switched to Delivery Services		Number of Customers Selecting Power Purchase Option		Percentage of Delivery Services Customers on Power Purchase Option (%)	
	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>
ComEd	16,422	996	6,422	288	39.1	28.9
Illinois Power	1,032	77	1,014	57	98.3	74.0
Total	17,454	1073	7,436	345	42.6	32.2

⁸ Provisions in Sec. 16-110 appear to require at least some electric utilities to offer a PPO product after 2006. However, the prices, terms and conditions under which the service would be offered might be different than existing prices, terms and conditions.

⁹ In its Order in Docket No. 02-0479, the Commission permitted ComEd to designate customers with a demand exceeding 3 MW as a competitive customer class.

Table 5: Amount of Usage Switched to the Power Purchase Option During 2003

<i>Utility/ Demand Level</i>	Amount of Usage Switched to Delivery Services (Thousand mWh)		Amount of Usage Switched to Power Purchase Option (Thousand mWh)		Percentage of Delivery Services Usage on Power Purchase Option (%)	
	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>	<i>Less than 1 MW</i>	<i>Greater than 1 MW</i>
ComEd	10,248	15,217	3,078	2,899	30.0	19.1
Illinois Power	736	4,843	731	2,317	99.3	47.8
Total	10,984	20,060	3,809	5,216	34.7	26.0

C. Retail Electric Supplier (“RES”) Activity

The list of eligible suppliers is comprised of Alternative Retail Electric Suppliers, which must obtain a certificate from the Commission before serving customers, and electric utilities serving outside their service areas. These entities are collectively known as “Retail Electric Suppliers.”

About 15 RESs are permitted to sell power and energy to retail electric customers in Illinois. Twelve RESs sold power and energy to retail customers in 2003, about the same number as in 2002.

As shown in Table 6, most suppliers have concentrated their marketing efforts in the ComEd service territory. However, suppliers are slowly beginning to offer service in the Ameren service areas. The smallest service areas have seen only a negligible amount of marketing activity.

Table 6: Number of Active Retail Electric Suppliers During 2000-2003, by Service Territory

Service Area/Year	2000	2001	2002	2003
AmerenCILCO	0	0	0	1
AmerenCIPS	3	2	4	5
AmerenUE	1	0	0	1
ComEd	8	7	8	8
Illinois Power	4	3	4	3
MidAmerican	1	1	0	0
All Others	0	0	0	0

D. Residential Market Activities in 2003

The Commission has not received any applications for certification to serve the approximately 4.4 million eligible residential customers. Suppliers have cited relatively high transactions costs as one reason why they may not direct their marketing efforts towards residential customers, at least in the near term. In particular, the cost of marketing to small-use, individual customers is high compared to the potential profit margin that a supplier might expect to receive by serving a residential customer. The Commission has attempted to address the problem of supplier transaction costs through its adoption of rule 83 Illinois Administrative Code Part 453 "Internet Enrollment Rules."¹⁰ This rule enables electric suppliers to use their Internet web sites to enroll customers, a procedure commonly used by market participants in other industries to minimize transaction costs.

IV. Conclusion

A significant number of customers in the four largest service areas of the State (AmerenCILCO, AmerenCIPS, Commonwealth Edison and Illinois Power) are taking advantage of the opportunities presented by customer choice to reduce their electric costs by switching to unbundled generation services. Despite the activity in these areas, however, there are a number of problems facing the development of healthy competition for retail electric power in Illinois.

First, with the exception of some recent activity in the AmerenCILCO and AmerenUE service areas, no other service areas are being served by Retail Electric Suppliers. Further, suppliers have shown little interest in serving residential customers. Second, the PPO offering is still a popular service offering in the service territories of ComEd and Illinois Power, the only two utilities that still offer PPO service. From a long-run perspective, customer reliance on the PPO as a strategy to save money is worrisome because the PPO will only be available to customers through the end of 2006, at least in its present form. Third, as discussed in the Commission's most recent Sec. 16-120(a) report to the General Assembly, the Commission is concerned that the lack of competitiveness in wholesale markets will affect retail market development.

The Commission's report noted that problems in the wholesale market include affiliate ownership of generation, limited transmission capability and high market concentrations in generation ownership. Since most electric utilities will purchase from the wholesale market much of the power they need for their bundled customers in 2007 and beyond, problems in the wholesale market will create problems in the retail market as soon as 2007, when the existing rate freeze expires. The Commission's report also

¹⁰ See Docket No. 02-0290.

contains a number of legislative recommendations that the Commission believes would enhance the prospects for a competitive wholesale market.